STATEMENT OF KARL E. BAKKE, CHIEF COUNSEL, MARITIME ADMINISTRATION, DEPARTMENT OF TRANSPORTATION, BEFORE THE SUBCOMMITTEE ON MERCHANT MARINE OF THE HOUSE MERCHANT MARINE AND FISHERIES COMMITTEE ON OVERSIGHT OF THE CITIZENSHIP REQUIREMENTS FOR ENGAGEMENT IN THE U.S. COASTWISE TRADES.

JUNE 22, 1989

Mr. Chairman and members of the Subcommittee, my name is Karl E. Bakke. I am Chief Counsel of the Maritime Administration, an agency of the U.S. Department of Transportation.

Because this hearing is one of a series concerning oversight of the Jones Act (section 27 of the Merchant Marine Act, 1920), I wish to reaffirm the Bush Administration's firm commitment to preserving the integrity of the Jones Act. U.S.-owned and manned ships in the coastwise trade move more tonnage than in the foreign trade, and have a significant impact on employment for thousands of seamen and workers in United States shipyards, ports and terminals. Also, these U.S.-citizen owned and manned ships are most immediately available in time of national emergency.

The Jones Act prohibits the transportation of merchandise by water between points in the United States in any vessel other than one (1) built in the United States, (2) documented under the laws of the United States, and (3) owned by citizens of the United States. A section of the 1920 Merchant Marine Act incorporates by reference the definition of citizen of the United States found in section 2 of the Shipping Act, 1916.

Although the Maritime Administration is not precluded under section 9 of the Shipping Act, 1916 from approving a demise or bareboat charter to a noncitizen for operation in the Jones Act trade, a policy was adopted in 1975 of not approving such charters to noncitizens. Since a demise or bareboat charterer assumes many of the indicia of ownership, including possession and direct control, the reason for not approving such charters in the Jones Act trade is apparent.

Section 2 provides, among other things, that for a corporation, partnership, or association "operating any vessel in the coastwise trade the amount of interest required to be owned by citizens of the United States shall be 75 per centum."

The one exception to the seventy-five percent U.S.-citizen ownership requirement for corporations owning or operating vessels in the Jones Act trade is found in the "Bowaters Amendment." Under the "Bowaters Amendment," corporations that have met the requirements of Section 27A of the 1920 Merchant Marine Act may own and document certain vessels for carriage of their <u>own</u> cargoes as well as those of a parent or subsidiary corporation.

The United States Coast Guard determines who is eligible to own a documented vessel with coastwise trading privileges. For purposes of determining such eligibility, the United States Coast Guard looks to the section 2 definition of citizenship. The

United States Customs Service is responsible for enforcing the requirements of the Jones Act. The Maritime Administration's role in determining U.S. citizenship, pursuant to section 2, relates more directly to the various promotional programs provided in the Merchant Marine Act, 1936 and to transactions involving transfer of an interest in or control of a documented vessel to noncitizens.

For example, in order to be eligible for a loan guarantee under Title XI, a recipient or transferee must be and must remain a U.S. citizen. If the recipient's vessels are to be used in the Jones Act trade, at least seventy-five percent U.S. ownership must be established to the satisfaction of the Maritime Administration. Under MARAD's citizenship regulations, a corporation must file an affidavit, setting forth names and citizenship of the president or other chief executive officer, the chairman of the board of directors, and all other directors. No more than a minority of the number of directors needed for a quorum can be noncitizens. Further, we require any person who is authorized to act in the absence, disability or inability of the president, chief executive officer or the chairman of the Board to be a U.S. citizen. The Congress has been aware of these requirements for at least 30 years, having been advised of our practice during hearings in 1959 on H.R. 6888 of the 86th Congress.

In addition to individual citizenship requirements for officers and directors, we have implemented three methods of establishing compliance with ownership requirements for U.S. corporate citizenship. The first is based on actual citizenship of stockholders (whether individuals or business entities) and the percentage of shares they own. The second method is based on the so-called "fair inference rule," which can be used by corporations whose stock is publicly traded and widely held. This alternative was judicially approved more than 50 years ago (Collier Advertising Service, Inc. v. Hudson River Day Line, 14 Fed. Supp. 335 (S.D.N.Y. 1936)); and is based on the premise that if 96 percent of the stock of a corporation is held by persons having registered U.S. addresses, then one can infer not less than seventy-five percent actual ownership by U.S. citizens. Finally, to protect the Jones Act eligibility of their vessels, some companies have adopted the practice of issuing legended certificates; "domestic shares" to citizens and "foreign shares" to noncitizens, with a restriction in the corporate charter on issuance of foreign shares in excess of the Jones Act limitation on noncitizen ownership. The Maritime Administration also accepts this third method as proof of U.S. citizenship.

Another criterion of citizenship under section 2 is the "controlling interest" test, that is applied separate and apart

from the economic test of ownership. If, by voting control or otherwise, noncitizens can exercise more than a 25 percent influence on the management or policies of a business entity, that entity will not be considered to be a U.S. citizen.

It should also be noted that the Maritime Administration looks to parent entities in determining ownership or control of a vessel-owning or -operating subsidiary. If the vessel owner or operator is ultimately owned or controlled by upstream "parent" entities, each "parent" entity must meet the citizenship requirements of Section 2.

The "controlling interest" test in the Maritime Administration's citizenship requirements is not applied by United States Coast Guard in its citizenship determinations for vessel documentation purposes, unless a license or endorsed registry for operating in the coastwise trade is being sought. The principal reason for this dichotomy, other than the fact that it is a statutory distinction, is that the 1936 Merchant Marine Act conditions access to maritime promotional programs, such as Title XI financing guarantees and operating-differential subsidy, on U.S. citizenship of the recipient. Obviously, it would be contrary to the policy and purposes of the 1936 Act to extend such benefits to a vessel-owning entity that may be wholly owned by noncitizens, even though its vessels may be entitled to the other privileges of U.S. documentation in foreign trade.

Although the principal focus of my remarks so far has been on corporate citizenship, MARAD views section 2 as imposing comparable economic and "controlling interest" requirements for citizenship of partnerships, associations, and other business entities, with variations due to the nature of the entity. For example, in the case of partnerships, MARAD requires all general partners to be section 2 citizens because under most, if not all, State laws a general partner can bind the partnership no matter how small a participation the general partner has. I might also say that this citizenship test for partnerships is consistent with the statutory requirement for documentation purposes.

This concludes my statement, Mr. Chairman. I will be happy to answer your questions and those of the other members of the Subcommittee.